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OGI International Financial Situation Report #23
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SOUTH AMERICAN REGIONAL DEBT DEVELOPMENTS

After a temporary respite, discussions are again being held about joint action by South American debtors. [redacted] 25X1 Ecuador is urging Latin American and Caribbean countries to devise a common position to solve the region's financial problems to be discussed at an upcoming conference in Quito during January. Ecuador hopes to build the consensus for a united front to press foreign bankers to ease repayment terms. [redacted] 25X1 [redacted] 25X1 the Ecuadoreans are proposing longer repayment terms with extended grace periods, a ceiling on debt servicing determined by the level of export earnings, easier IMF adjustment programs, and the development of new mechanisms by Latin central banks to exchange information on debt renegotiations. [redacted] 25X1

Thus far, few Latin debtors have reacted to these proposals. Although the Brazilians support easier repayments, we believe they will not favor an action that would interfere

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with their trade policies. Moreover, the exchange of information among central banks has drawn Brazil's ire because of its potential to be misconstrued as a debtor's cartel by foreign creditors. Unless one of the major debtors actively supports these proposals, we expect this conference to produce few concrete results toward unifying the Latin debtors. 25X1

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Although we believe that collective action still remains unlikely, a new initiative by former Peruvian Economic Minister Ulloa bears watching. Acccording to the US Embassy in Lima, he is urging Argentina to spearhead negotiations with creditors aimed at turning short-term credits into longer-term, low-interest debt. The Embassy in Buenos Aires reported, however, that the Peruvian approach is being resisted by Argentine financial officials who have lobbied against Alfonsin's accepting a central role in bloc debt negotiations. We concur with the US Embassy in Lima that these developments are serious, but are not expected to lead to a confrontation at the Quito meeting. 25X1

The January meeting, however, will provide the Latin debtors an opportunity to vent their growing dissatisfaction with IMF austerity. According to numerous Embassy reports, most Latin debtors object to IMF stand-by accords which require rapid balance-of-payments reversals at the expense of domestic economic growth and slashed social welfare expenditures.

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Venezuela is trying to bypass the IMF in its rescheduling negotiating with creditors. Peru and Bolivia--as well as Costa Rica, Jamaica, and the Dominican Republic--are facing difficulties in negotiating with the IMF for 1984 agreements and may not resume talks before the Quito January meeting. Argentina, currently out of compliance with its Fund program, is expected to start negotiations early in the year and will likely press for IMF accommodations on spending limits. [redacted] 25X1

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ARGENTINA

Commercial bankers disbursed $500 million to Argentina on 1 December after some hurried last-minute work by the bank advisory committee. The funds were made available this month, in spite of Argentina's non-compliance with IMF, as a goodwill gesture to the Alfonsin government which took office on 10 December. The new funds will be used to make the first payment against a $1.1 billion bridge loan and to cover interest arrears through mid-October 1983. The elimination of arrears from the loan proceeds will allow US banks to avoid placing numerous loans to Argentina in a non-accrual status. The bank disbursement was the first tranche of a $1.5 billion medium-term loan promised earlier in the year, but the remainder will be held up pending renegotiation or a new agreement with the IMF. [redacted] 25X1

The incoming civilians have yet to spell out a complete set of economic policies, [redacted] 25X1 25X1

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stimulative policies and intervention in exchange and foreign trade markets may delay an agreement with the Fund, necessary to elicit the $4 billion in new loans the Embassy expects Argentina to require in 1984. [redacted] 25X1

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BRAZIL

The IMF's approval of Brazil's revised stabilization program on November 22 restored critically needed foreign financial support. In return for commitments on more restrictive fiscal, monetary, and wage policies, the IMF and foreign banks released suspended payments totaling $3.2 billion. Most of these funds have been used to repay bridge loans obtained from the Bank for International Settlements and other banks in late-1982. Despite these repayments, Brazil's financial straits remain serious. New loan funds will be needed to clear up some $3 billion in interest and other payments arrears, rebuild reserves, and bolster Brazil's liquidity position--the objectives of Phase II. [redacted] 25X1

Brazil's new financial rescue package, however, is faltering somewhat. [redacted] 25X1 according to the US Embassy, foreign government contributions to a pledged $2.5 billion export credit remain in doubt. [redacted] 25X1

Difficulties in finalizing Phase II likely will not impede

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Brazil's ability to clear up its present arrears by the end of the year but may lead to a renewed foreign exchange crunch in early 1984. [redacted] the major banks 25X1 still appear willing to provide a bridge loan to prevent the risk of any US banks declaring existing loans non-performing after December 31. Delays in implementation, however, augur difficulties late in the first quarter, a time when export earnings usually are low and debt service payments high. If the banks fail to subscribe to the full $6.5 billion target amount, the entire process of obtaining funding commitments may have to be reinitiated. [redacted] 25X1 We believe if no major additional payments are made by the end of the first quarter, large new arrearages are almost certain. [redacted] 25X1

Meanwhile, financial circles both in Brazil and foreign capitals increasingly believe that Brasilia will not be able to adhere to the recently revised IMF program. [redacted] 25X1 We share that concern. According to the US Embassy in London, an internal Brazilian working government report has described the balance of payments targets used in

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the stabilization program as already looking hopelessly optimistic. Among recent events that may have discouraged Brasilia's officials are a constitutional tax amendment passed by a the Congress which the US Embassy says will result in a loss of some 3 percent of Brasilia's tax revenues next year, and the Sao Paulo metalworkers and autoworkers unions wage settlements that have exceeded the new salary guidelines. If Brazil is unable to reduce substantially its high-flying inflation rate and once again falls out of compliance with IMF terms, Phase II financing will likely fall far short of the country's needs and another period of intense economic and political turmoil will ensue. [redacted] 25X1

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ECUADOR

Ecuador met recently with its creditors to discuss 1984 financial needs. [redacted] 25X1 Because Ecuador remains in compliance with 1983 IMF program targets, we believe it may gain access to new funds and eliminate its $250 million arrearages. To retain bankers support, however, Ecuador also will have to finalize the plan to convert private debt from dollars to sucres and reach a new agreement with the Fund in the spring during the heat of the electoral campaign. [redacted] 25X1

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PERU

Lima's deteriorating fiscal position and continued large military outlays are generating problems with the IMF and commercial banks which could upset Peru's financial rescue package. According to Embassy reports, the government is now renegotiating targets under the IMF program because it failed to reduce the public deficit as stipulated in the agreement. Instead, Peru's federal deficit doubled to 9 percent of GDP this year because of (a) the fall in tax revenues induced by the 10 percent decline in economic activity, (b) the higher public spending necessitated both by the increase in inflation to 130 percent and programs to blunt the impact of natural disasters, and (c) inablility to trim military and security outlays. [redacted] 25X1

Dismayed by Lima's failure to comply with the IMF program, international lenders are now delaying some project loan disbursements, notably a $200 million World Bank structural adjustment loan. [redacted] 25X1

As a result of these loan delays, Lima has likely been forced to cover its $1.1 billion current account deficit through reductions in its foreign reserves by more than the IMF agreement permits. Failure to get the IMF program restarted

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soon--a task now made more difficult by rising domestic opposition to austerity and the planned departure of the finance minister next month--will jeopardize more than $800 million in commercial bank rescheduling and new loans arranged earlier this year, nearly $700 million pending under the Fund agreement, and Lima's ability to obtain $400 million in new loans it claims to need in 1984. [redacted] 25X1

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